LIBRARY
SUPREME COURT, U. S.

FILED
MAY 7 1968
JOHN F. DAVIS, CLERK

No. 1250

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

GENERAL FOODS CORPORATION, *Petitioner*

v.

FEDERAL TRADE COMMISSION, *Respondent*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITIONER'S REPLY BRIEF

ROBERTS B. OWEN
701 Union Trust Building
Washington, D. C. 20005
Attorney for Petitioner,
General Foods Corporation

Of Counsel:

GERALD P. NORTON
G. JOSEPH VINING
COVINGTON & BURLING
701 Union Trust Building
Washington, D. C. 20005

KENDALL M. COLE
250 North Street
White Plains, New York

INDEX

	Page
Argument	1
Conclusion	13

CITATIONS

Brown Shoe Co. v. *United States*, 370 U.S. 294 (1962) 3, 4, 5

Federal Trade Commission v. *Procter & Gamble Co.*, 386 U.S. 568 (1967) ..... 5, 6, 8 n.6, 11, 12 & n.8

St. Joseph Stock Yard Co. v. *United States*, 298 U.S. 38 (1936) 12

United States v. *Continental Can Co.*, 378 U.S. 441 (1964) ... 5

United States v. *El Paso Gas Co.*, 376 U.S. 651 (1964) 5

United States v. *Penn-Olin Co.*, 378 U.S. 158 (1964) 5

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 1250

GENERAL FOODS CORPORATION, *Petitioner*

v.

FEDERAL TRADE COMMISSION, *Respondent*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITIONER'S REPLY BRIEF

ARGUMENT

The brief in opposition filed by the Government seems to be misdirected. It simply does not address itself to the questions raised by petitioner.

In this respect the tone is set in the first half of the brief, the nine-page "Statement" of the case. It is quite apparent that the propositions included in the Statement were selected, not on the basis of their relevance to the issues raised in the petition, but in an effort to create the impression that the result below, no matter how reached, was correct. Included are a number of

questionable assertions, but because the Statement as a whole is almost entirely irrelevant to the only three points at issue, we will not burden this reply brief with a complete response.[1]

Similarly, the "Argument" largely misses the point. The petition raised three significant issues of antitrust law. As to *each,* the brief mischaracterizes the point and, having thus created a straw man, knocks it down. In the process, since the brief does not speak to the issues raised by the petition, the Government has failed to make a case against the importance of the issues or the appropriateness of their review by this Court.

1. The Government's position on the first point is basically that petitioner's position here is "merely a reassertion, in slightly altered form, of the market definition argument which it advanced unsuccessfully" below. (Br. 9) Conceiving the first issue thus, the Government then portrays GF's argument as merely a factual attack on the factual conclusions reached below

[1] Two or three examples will show that the propositions asserted in the Statement must be viewed with caution: (1) A considerable effort is made to create the impression that there are enormous obstacles, technological and otherwise, to entry into the steel wool business. (Br. 4-5) In fact, the record shows that it is relatively inexpensive and easy, even for persons with no steel wool manufacturing experience, to enter and succeed in the market. (R. 229a, 565a, 588a, 613-14a, 640a, 966a) (2) The brief also attempts to create the impression that after and as a *result* of the merger S.O.S.'s market share increased substantially. (Br. 8) In fact the Examiner found, with the apparent approval of the Commission, that the increase in market share was brought about by developments unrelated to GF's ownership of the business. (R. 176a, 208a n. 8) (3) The brief attributes certain motivations and thought processes to Brillo, S.O.S.'s principal competitor, as though there were evidence in the record as to Brillo's reactions to the merger (Br. 8), but in fact there was no evidence whatever as to Brillo's reactions to GF's presence in the market.

on the market definition question, and on this basis the Government undertakes an extended and frequently doubtful factual justification of those conclusions.[2] But of course GF here has not attacked those conclusions at all, and the Government's attempted justification of the market definition adopted below is completely beside the point.

The difference between the parties on this portion of the case lies in the distinction between two different tasks which must be undertaken by the deciding tribunal in a conglomerate merger case. An important preliminary task, of course, is that of defining the relevant product market or submarket according to the criteria laid down in this Court's decision in *Brown Shoe Co.* v. *United States,* 370 U.S. 294, and related cases. The function requires an examination of existing products and the methods then prevailing in their

---

[2] Examples of the Government's handling of the facts are as follows: (1) The brief asserts that the Commission found that the prices of non-steel substitute products were "independent of those of steel-wool soap pads." (Br. 11) The Commission did not so find. In fact the Examiner below found, on the basis of uncontroverted evidence, that the prices of the substitute products were based directly on steel wool prices (R. 171a; *see* R. 535a, 785a, 893a, 895a), and the Commission affirmed that finding. (R. 208a n. 8) (2) The brief asserts that "in the ten-year period since the acquisition" GF-S.O.S. made only a single price change, and that that change was a price increase. (Br. 12) There was a price increase in 1958, a few months after the acquisition, but it was the direct result of an increase in the price of steel (R. 945a), and thereafter, as Commission counsel emphasized in the Court of Appeals, there were frequent competitive price reductions. (Brief for Respondent at 59) (3) The Government attempts to brush aside the recent decline in steel wool soap pad sales by saying in effect that the affidavit which establishes that decline does not indicate that the decline has been caused by substitute products. (Br. 12 n. 1) In fact the affidavit states explicitly that the substitute products have been "[a]n important factor in bringing about the foregoing reversal . . . ." (Pet. App. C. p. 4)

production and sale (*e.g.*, "the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors"; 370 U.S. at 325). This evaluation of existing products was undertaken by both of the lower tribunals in this case, and all of the commissioners and judges who expressed their views (including Commissioner Elman) agreed on the market definition. As the petition makes clear, the propriety of the market definition below is simply not at issue here.

What *is* at issue is whether the lower tribunals, having completed their market-definition function, could then treat as irrelevant affirmative evidence of emerging substitutional competition—or whether they had an additional responsibility with respect to that subject matter. The Government's position is that, once the market has been defined under the *Brown Shoe* criteria, no further consideration need be given to substitute products for any purpose. But Commissioner Elman put his finger on the error in this position. He pointed out that an additional and quite distinct inquiry with respect to substitute products remained—namely, the task of evaluating the emerging role of any potential competition that might exist in the form of companies engaged in the development of substitutional products for the future:

> "In its decision today, the Commission ignores the nonsteel wool products and the competition which they represent to firms in the steel wool market. The Commission justifies this on the ground that the 'relevant market' does not include these other products. But, as I have pointed out, the critical question in this case is that of determining whether, and to what extent, this merger will bring about 'deep underlying structural

> changes' substantially lessening competition in the steel wool market. *If, as the Commission holds, the legality of this merger must be judged by measuring its effects on potential competition, how can we close our eyes to anything that, as a matter of marketing reality, constitutes potential competition to firms in that market?* (Pet. App. B., p. 257a) (Emphasis added.)

Commissioner Elman also made clear that this second function, the evaluation of the role of the potential competition of emerging substitutes, requires a consideration of a number of economic factors (*e.g.*, the size, aggressiveness, marketing prowess, and history of success of the manufacturers of the emerging substitutes, the probable psychological impact in the future upon companies within the market, etc.) which are outside the scope of the problem of market definition under *Brown Shoe*.[3] These economic factors must be weighed in accordance with the standards announced by this Court in *El Paso, Penn-Olin, Continental Can,* and *Clorox,*[4] rather than the market definition criteria previously laid down in *Brown Shoe*. The latter criteria were never intended for this purpose. In other words, the second function involves a kind of inquiry which is entirely distinct from the only inquiry undertaken by

---

[3] The Government's brief makes an effort to portray the disagreement between Commissioner Elman and his brethren as merely a disagreement as to the "evaluation of the evidence" and "the inferences to be drawn from the evidence" (Br. 10, 11), but the issue was and is far more fundamental. The Commission majority regarded potential competition in the form of emerging substitutional products as irrelevant as a matter of law, and Commissioner Elman quite properly disagreed as a matter of legal and economic principle.

[4] United States v. El Paso Gas Co., 376 U.S. 651 (1964); United States v. Penn-Olin Co., 378 U.S. 158 (1964); United States v. Continental Can Co., 378 U.S. 441 (1964); FTC v. Procter & Gamble Co., 386 U.S. 568 (1967).

the tribunals below—and in this respect the only point at issue is whether those tribunals had a duty, as a matter of law, to undertake the second inquiry as well as the first.

To the extent that the Government's brief comes to grips with this issue at all, its argument seems to be this: that, although under *Clorox* the role of potential competition generally is crucial in conglomerate merger cases, potential competition in the form of substitutional products is *not* relevant except insofar as it may be taken into account in identifying the existing products to be included in the relevant product market. In other words, if existing competition from substitutes is not "actual" enough to be included within the relevant product market at the time that market is defined, then it is legally unnecessary to take emerging substitutional competition into account as a future restraining influence upon the exercise of oligopoly power within the market. This position, upon which the decisions below stand or fall, is, we submit, so economically unsound, so inconsistent with this Court's realistic analyses in prior potential competition cases, and so damaging to the antitrust treatment of conglomerate mergers, that this Court should grant certiorari.

2. On the second question raised by the petition the Government has again mischaracterized the point. The brief in opposition states that petitioner's contention "appears to be" that a merger which raises entry barriers "is illegal *only* if barriers are raised high enough to keep out *every* potential entrant, no matter how large and powerful." (Br. 13) (Emphasis added.) Having thus reconstructed petitioner's argument, the Government proceeds to demolish it, but, since the attributed argument is both absurd and non-existent, the Government's discussion of it totally misses the point.

The question actually raised in the petition is simply this: where a merger is said to have raised entry barriers to a certain extent, but where significant potential competition has survived, does the raising of the barriers (to the extent that it has occurred) *ipso facto* establish a substantial lessening of competition and end the inquiry—or is it necessary for the deciding tribunal to go on to evaluate the influence of the potential competition which has survived? The Court of Appeals below took the first step, but it refused to take the second.

The court's error, and the error underlying the Govment's position here, both stem from a failure to recognize that the significant question in entry barrier analysis is not whether the challenged merger has in fact made it more difficult for one firm or another to enter the market, but whether the merger has substantially diminished the influence of potential entrants, taken as a group, as a restraining (*i.e.*, psychological) influence upon firms within the market. For example, it would be perfectly possible for a particular conglomerate merger to affect the private plans of one potential entrant or another without really diminishing the influence of potential competition as a whole. That being so, it is not sufficient to argue, as the Government does, that "*some* companies" outside the steel wool market may have been discouraged from entry to some unspecified extent by the challenged merger. (Br. 14)[5] The essential inquiry remains whether, given the number, size, market power, etc., of

[5] In fact the Government's argument is based on pure speculation; there is no evidence that any potential entrant was actually discouraged from entry by the merger. Indeed, the evidence is to the contrary: three companies have entered the steel wool market in the post-acquisition period. (*See* Pet. 12)

identified potential entrants remaining after the merger, the companies in the market would feel less constrained than before.

The Court of Appeals below failed (in the Government's view properly) to undertake that inquiry. Indeed, of the eight individuals who participated in the decisions below, only one—Commissioner Elman—really considered the question, and his conclusion was clear. Having in mind the character of the potential competitors remaining on the scene after the merger ("with their vast resources and marketing power" Pet. App. B., p. 258a), he said:

> "Whatever potential competition was eliminated is of paltry significance compared to what remains: and there is every indication that potential competition will increase, rather than decrease, in the future. To the extent that the possibility of new entry acts as a restraining influence on sellers in an oligopolistic or concentrated market, inclining them to maintain prices at a level low enough to discourage entry (see *Clorox*, pp. 27-28, 61-62), the acquisition here cannot be regarded as affecting potential competition in any way that could reasonably be expected to influence the behavior of S.O.S., Brillo, and the other firms in the steel wool business. . . ." (Pet. App. B, pp. 255a-256a)

In its brief the Government attempts a factual attack upon Commissioner Elman's conclusion (Br. 13-14),[6]

---

[6] In fact the attack itself is based on a misreading of the record. The Government asserts in effect that there is no evidence that any of the large identified potential competitors had any interest in the steel wool soap pad market (Br. 13-14)—whereas the cited portions of the record show that Colgate-Palmolive is actively engaged in the steel wool soap pad business, that Lever Bros., American Home Products, and Procter & Gamble have shown an interest in the development of steel wool soap pads, and that Union Carbide, the du Pont Company, General Mills, General Cable and

but, whatever the merits of the factual argument, it cannot excuse the Court of Appeals' refusal to consider the character and strength of the identified potential entrants whose influence would continue to be felt in the future. Where there has been no consideration of such factors, there is no basis for concluding that there has been a reduction in the restraints upon the exercise of oligopoly power within the market and hence a lessening of competition within the meaning of Section 7.

3. The third issue raised by petitioner is whether the achievement of genuine economic efficiencies as a result of a conglomerate merger can properly be treated as an affirmative basis for condemning the merger. The striking feature of the Government's position with respect to this question is that at no point does it disagree with petitioner as to the correct answer to the question as a matter of law. It is evident that in this Court (though not before the Commission or the Court of Appeals) the Government concedes that real efficiencies are not a proper basis for condemning such a merger.

Having confessed as much, however, the Government attempts to avoid the consequences here by asserting that in this case the achievement of economies in transportation and distribution "was not the basis of the Commission's decision." (Br. 15) The issue between the parties now, therefore, is not the importance of the efficiencies question or what its proper resolution should be; the issue is what was said in the opinions below.

Minnesota Mining are all either interested or actively engaged in marketing closely related products. *Cf.* FTC v. Procter & Gamble Co., 386 U.S. 568, 573, 580 (1967).

Obviously that dispute can be readily resolved simply by reading the opinions and briefs. Counsel supporting the complaint before the Commission vigorously argued that GF's acquisition of S.O.S. had allowed the resulting company to achieve economies of scale in transportation and distribution—and the Commission majority's opinion repeatedly refers to such economies as affirmative reasons for condemning the merger. These factors, together with resulting reductions in operating costs and prices to retailers, are described in great detail in the lengthy appendix to the Commission's decision, and on this basis Commissioner Elman correctly observed that "[t]he Commission also includes, as a ground for holding this merger unlawful, purported cost savings accruing to S.O.S. through efficiencies in warehousing and distribution." (Pet. App. B, p. 261a) Thereafter, at the explicit request of Commission counsel, the Court of Appeals below rejected Commissioner Elman's and petitioner's objections to the majority's position and expressly mentioned the controversial cost savings as a ground for sustaining the Commission majority's decision. (Pet. App. A, p. 19) In the opinions below there is thus a clear condemnation of economies of scale, and the Government is simply wrong in suggesting the contrary.[7]

---

[7] The Government also attempts to minimize the significance of these efficiencies by asserting that they "are *not* production or distribution efficiencies that would be available to any firm ... . but advantages available to a particular competitor only because of its sheer market power." (Br. 16 n. 3) It attempts to support this proposition by focusing entirely upon advertising and promotional cost savings. But the efficiencies involved in *this* case include actual distribution efficiencies such as "a market center distribution system," "warehousing by the most efficient time and labor-saving devices," and "distribution by the most advantageous rate of transportation," enabling a retailer to "run his business more economically by holding his investment and inventory to a minimum." (*See* Pet. 14-15)

Going to really rather remarkable lengths to avoid these difficulties, the Government then observes that operating efficiencies "cannot justify an otherwise unlawful merger," thus creating the impression that such economic efficiencies were brought into the case by petitioner by way of defense, rather than by Commission counsel as a ground of illegality. (Br. 16) This is untrue. Such efficiencies were brought into the case by counsel supporting the complaint. They affirmatively sought to prove the existence of cost savings in transportation and distribution and leaned heavily on such evidence before both the Commission and the Court of Appeals. And in this effort, as noted, they were successful. At no time has petitioner ever relied on such evidence as a defense.

Apart from the foregoing attempts to avoid the issue raised in the petition, the Government advances the extraordinary suggestion that, even if the Commission below relied upon invalid grounds for condemning this merger, this Court should not consider such invalid grounds because the Commission also took into account grounds which the Government considers valid. The theory rests upon two propositions: (a) that the economics of this case and *Clorox* are substantially identical (an approach which Commissioner Elman described as the "carbon copy" approach (Pet. App. B, p. 251a)) and (b) that, since the foregoing conclusion must be regarded as unassailable, it is immaterial that the Commission also relied upon economic efficiencies—a ground which the Government characterizes as being not "essential to its holding of illegality." (Br. 16) But this line of argument is totally unacceptable.

In the first place, the initial proposition begs the question. With respect to each of the three issues presented here, petitioner asserts that the tribunals below misinterpreted, and acted inconsistently with, the

teachings of *Clorox*. We claim, as Commissioner Elman put it below, that this case is not a "mere replica" of *Clorox* (Pet. App. B, p. 249a) and that the Commission here has moved significantly "beyond the existing boundaries of the merger law." (*Ibid.*)[8] Hence the Government's assertion that, on the "carbon copy" ground alone, the Commission "was justified in condemning the present merger" (Br. 15-16) is hardly an argument that the case is not sufficiently important to be considered by this Court.

Secondly, and for present purposes more significantly, it is hornbook law that an administrative decision reached in reliance upon improper considerations cannot stand, regardless of any speculation about what that decision might have been in the absence of those considerations. *E.g., St. Joseph Stock Yards Co.* v. *United States,* 298 U.S. 38, 75 (1936). Since the Government in effect here concedes the impropriety of reliance upon genuine economies to invalidate a merger, and since the point is of great significance in the administration of the antitrust laws, certiorari should be granted.

CONCLUSION

Petitioner contends that the tribunals below reached their conclusion by refusing to consider legally relevant factors, and by taking into consideration, and relying upon, legally irrelevant matters. The legal rules thus put in issue in this case are of great importance to the antitrust laws, and the Government's

[8] Since the significant economic differences between this case and *Clorox* have been noted by Commissioner Elman (Pet. App. B., pp. 252a-55a), by the Court of Appeals (Pet. App. A, pp. 20-21), and in the petition (Pet. 4-5), they need not be repeated here.

difficulty in dealing with them confirms petitioner's conclusion that the petition for certiorari should be granted.

Respectfully submitted,

ROBERTS B. OWEN
701 Union Trust Building
Washington, D. C. 20005
Attorney for Petitioner,
General Foods Corporation

Of Counsel:

GERALD P. NORTON
G. JOSEPH VINING
COVINGTON & BURLING
701 Union Trust Building
Washington, D. C. 20005

KENDALL M. COLE
250 North Street
White Plains, New York